**IN THE HIGH COURT OF JUDICATURE AT BOMBAY**

**ORDINARY ORIGINAL CIVIL JURISDICTION**

**INCOME TAX REFERENCE NO. 18 OF 1988**

The Commissioner of Income-tax, )
Bombay City-IX, Bombay. ) ...Applicant

V/s.

Shri Anil M. Gehi, )
Gehi Mansion, 100, L.J. Road, )
Mahim, Bombay-400 016. ) ...Respondent

Mr.A.N. Kotangle with Mr.D.A. Dubey i/b.K.C. Sidhwa for Applicant.

Mrs.Shobha Jagtiani i/b. D.M. Parikh for Respondent.

**CORAM : V.C. DAGA AND A.S. AGUIAR, JJ.**

**DATED : AUGUST 19, 2005.**

**ORAL JUDGMENT (PER A.S. AGUIAR, J.) :-**

. The following question of law arising out of the order of the Tribunal in ITA No.5118/Bom/1985 dated 11th August, 1986, for the assessment year 1982-83 has been referred to this Court for its opinion, at the instance of the Revenue.

> "Whether, the foreign currency of Rs.4,56,980/- confiscated from the assessee was allowable as a loss to the assessee."

2. The matrix of facts giving rise to substantial question of law is as follows :-

. The assessee is an individual whose relevant account year ended on 31st March, 1982. He was proceeding to Hong Kong on 8th August, 1981. He was apprehended by the customs authorities at Bombay Airport and foreign currency equivalent to Rs.4,56,980/- was seized from his custody. The customs authorities questioned the assessee and his companion Aboobackar. The Additional Collector of Customs by order dated 16th August, 1982 confiscated the foreign currency seized from the assessee and further imposed fine of Rs.1,50,000/- on the assessee for contravening the Foreign Exchange Regulation Act. The order of confiscation is confirmed by the Customs, Excise and Gold Control Appellate Tribunal (CEGAT) by order dated 2nd May, 1984. On these facts, the ITO treated Rs.4,56,980/- as assessee’s income from undisclosed sources but rejected the assessee’s claim for the loss suffered by him.

3. The CIT (Appeals) upheld the ITO's order and distinguished the assessee's case from that of the **Piara Singh**'s case **(1980) 124 ITR 40** by pointing out that Piara Singh was admittedly a smuggler while assessee had denied the foreign currency belonged to him and therefore while the unexplained money was assessable under Section 69A, the loss of foreign currency due to confiscation was not allowable. The assessee appealed to the Tribunal and argued that the customs authorities had treated the assessee as smuggler and had confiscated the foreign currency and therefore, he was entitled to deduction of the loss. Alternatively, it was argued that even if the assessee was held not to be a smuggler, the fact remained that foreign currency found in the assessee's possession had been confiscated by the customs authorities. It was submitted that seizure of foreign currency is unexplained money of the assessee under section 69A. There was no justification for not allowing the loss of foreign currency. Accepting the contention of the assessee, the Tribunal held that there was no justification for disallowance of loss of foreign

currency which was confiscated and directed that the confiscated foreign currency of Rs.4,56,980/- be allowed as a loss to the assessee. The Revenue has, therefore, approached this Court for its opinion on the question of law which was originally proposed as follows :-

> "Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in holding that the foreign currency of Rs.4,56,980/- confiscated by the customs authorities from the assessee should be allowed as a loss to the assessee while assessing the same as unexplained income of the assessee under section 69A, in view of the fact that the source of such foreign currency has not been explained, as a result of which the income is assessable under the head "other sources" and not under the head "business or profession" and further, the loss of the amount due to the confiscation being in the nature of personal loss is not eligible for set off?"

. The Tribunal, however, has reframed the question as follows :-

> "Whether, the foreign currency of Rs.4,56,980/- confiscated from the assessee was allowable as a loss to the assessee."

4. The authorities below i.e. the Income Tax Officer and the Commissioner of Income Tax (Appeal) had noted the assessee's statement before the customs authorities denying ownership of the foreign currency seized and alleged ignorance as to how the same came into his possession. They also noted the rejection of the assessee's defence by the customs authorities and the order of confiscation of foreign currency seized from assessee and imposition of fine of Rs.1,50,000/- on the assessee for contravention of the Foreign Exchange Regulation Act. It was also noted by the ITO as well as the CIT (Appeals) that the customs authorities did not accept the story of the assessee as the assessee was not able to satisfy the customs authorities that he was not the owner of the money seized. In view thereof, the ITO

and CIT (Appeals) ordered that the sum of Rs.4,56,980/- held in foreign currency and seized from the assessee be treated as unexplained income of the assessee subject to tax under Section 69A of the Income-Tax, 1961. **Section 69A provides as follows :-**

> "Where in any financial year the assessee is found to be the owner of any money, bullion, jewellery or other valuable article and such money, bullion, jewellery or valuable article is not recorded in the books of account, if any, maintained by him for any source of income, and the assessee offers no explanation about the nature and source of acquisition of the money, bullion, jewellery or other valuable article, or the explanation offered by him is not, in the opinion of the Income-tax Officer, satisfactory, the money and the value of the bullion, jewellery or other valuable article may be deemed to be the income of the assessee for such financial year."

5. In view of the non-satisfactory explanation given by the assessee to the customs authorities, as a result, the foreign currency came to be confiscated, the currency equivalent to the value of Indian Rs.4,56,980/- was deemed to be the income of the assessee for the Financial Year 1981-82 in which year the same was found with him.

6. The assessee claimed that he was entitled to have money confiscated treated as a loss which the tax authorities/revenue rejected. The assessee in claiming the loss of Rs.4,56,980/- had relied upon the decision of the Supreme Court in the case of **Piara Singh** (supra). However, both the ITO and CAT rejected the contention distinguishing the case of **Piara Singh** from the present case pointing out that **Piara Singh** was apprehended with the sum of Rs.65,000/- in hard currency notes while carrying on smuggling activities, while crossing the border between India and Pakistan. The assessee, on the other hand, has denied that the said foreign currency of Rs.4,56,980/- was his. In the case of **Piara Singh,** it

was held that the loss of currency was in the process of smuggling which was the business of **Piara Singh** and therefore, the confiscation of the money from **Piara singh** was treated as business loss. So far as the assessee is concerned, he, on his own showing, was not running any smuggling activity. In fact, he denied that he was the owner of the foreign currency and therefore, while the Revenue has treated the said amount as his income from undisclosed source under section 69A, it has rejected his claim for treating the said amount as a loss as smuggling admittedly was not the business of the assessee.

7. In appeal before the Tribunal, the assessee made the same submission and pointed out that according to customs authorities, he was treated as smuggler and therefore, foreign currency was confiscated. Alternatively, it was submitted that even if the assessee was held not to be a smuggler, the fact remain that the foreign currency found in his possession has been confiscated by the customs authorities. The Tribunal found that there was no justification for

assessing the foreign currency seized as unexplained money of the assessee under section 69A and at the same time, not allowing the loss of the foreign currency. The Tribunal, accordingly, allowed the appeal and directed the amount of foreign currency of Rs.4,56,980/- confiscated from the assessee be allowed as the loss to the assessee.

8. Before this Court, the submission of the Revenue was that since the assessee was not carrying on the business of smuggling, the amount confiscated from him under Section 69A would not be entitled to be treated as a business loss, as admittedly, the assessee was not carrying the business of smuggling. Reference has been made to the Judgment on the case of **Andhra Pradesh** High Court in the case of **Bijjala Shivalingam v. Commissioner of Income-Tax, (2002) 253 ITR 105** wherein it was held that -

> "In order to claim deduction of expenditure under section 37(1) of the Income-Tax Act, 1961, four conditions must be fulfilled, viz., (i) the

expenditure in question is not of the nature described under the specific provisions of sections 30 to 36; (ii) the expenditure is not of the nature of capital expenditure; (iii) it is not a personal expenditure; and (iv) the expenditure has been laid out or expended wholly or exclusively for the purposes of business or profession. Unless all the above four conditions coexist, the claim for deduction of expenditure under section 37(1) of the Act cannot be allowed."

9. In the said case, the assessee was carrying on business as a retail dealer in silver and silver articles. Assessee had no licence to deal in gold or gold ornaments. Assessee filed return of income for the year 1983-84. In the meantime, the Central Excise Authorities had conducted a search at the residential premises of the assessee on 5th May, 1982 and seized gold biscuits and jewellery articles valued at Rs.3,30,400/- and cash amounting to Rs.2,20,000/- in Indian currency. The value of the gold biscuits and

jewellery was treated as income of the assessee as undisclosed sources and accordingly, taxed under section 69A. The assessee filed an appeal contending that he was smuggling gold and hence, the value of gold biscuits and gold jewellery was deductible under section 37-2. His contention was rejected by the Tribunal. On reference, it was held that before the Customs and Central Excise Authorities, the Assessee had denied that he indulged in gold smuggling activities. In addition to that, the petitioner-assessee denied that the seized gold biscuits and gold jewellery belonged to him and claimed that they were kept in the almiragh by his brother. It is also relevant to note that the gold biscuits and gold jewellery were seized from residential premises of the petitioner-assessee and not from his business premises. In the circumstances, no inference could be drawn that the seized gold biscuits and gold jewellery formed part of the closing stock of the alleged illegal activity of smuggling gold. It cannot be said that the value of gold biscuits and gold jewellery viz. Rs.3,39,400/- was laid out or expended by the petitioner-assessee wholly or exclusively for the

purposes of his business or profession, therefore, it was not deductible as business expenditure. In the said case, the **Andhra Pradesh** High Court observed as follows:-

> "It is very pertinent to notice that in **Piara Singh's case (1980) 124 ITR 40 (SC); Shri Ram Chander's case (1986) 159 ITR 689 (P & H) and Prakash Chand Sushil Kumar's case (1989) 179 ITR 27 (P & H)**, the assessees were admittedly indulging in smuggling of gold. In **Piara Singh's case (1980) 124 ITR 40 (SC)** decided by the apex court, the assessee, Mr.Piara Singh, admitted that he was taking the currency notes to Pakistan to purchase gold there and smuggle it into India. In **Shri Ram Chander's case (1986) 159 ITR 689 (P & H)**, the assessee admitted that the seized gold bars were delivered to him by one Mr.Champath Rai of Rohtak for delivering the same to one Lalchand. In other words, the assessee admitted his smuggling activity. Similarly, in **Parkash Chand**

**Sushil Kumar's case (1989) 179 ITR 27 (P & H)**, it is apparent from the judgment that Mr.Sushil Kumar, one of the partners of the assessee-firm was carrying on smuggling of gold. In the context of the position admitted by the assessees themselves and also having regard to the findings recorded by the authorities under the Customs Act, the Supreme Court and the Punjab and Haryana High Court, allowed deduction under section 37 of the act as business or trading loss. The ratio of the above decisions of the Supreme Court and the Punjab and Haryana High Court is not applicable to the fact-situation of this case. We say this because, even according to the assessee himself he was not carrying on any smuggling activity."

10. The legal position has been finally set to rest by the decision of the Supreme Court in the case of **Commissioner of Income Tax v. Piara Singh reported in (1980) 124 ITR 40** wherein the Apex Court has confirmed the decision of Punjab & Haryana High Court in

**Commissioner of Income-Tax v. Piara Singh (1972) 83 ITR 678** and has disapproved the Judgment in the case of **J.S. Parkar v. V.B. Palekar (1974) 94 ITR 616 (Bom.)** and explanation given on **Soni Hinduji Kushali & Co. v. CIT (1973) 89 ITR 112 (AP)** and applied the principle laid down in the case of **Badridas Daga v. CIT (1958) 34 ITR 10 (SC)** and has also referred to its observation in the case of **CIT v. Kothari (S.C.) (1971) 82 ITR 794 SC.** In applying the principle laid down by it in **Badridas Daga** while upholding the Judgment of the Punjab & Haryana in **Piara Singh**'s case, the Apex Court noted as follows :-

> "In our judgment, the High Court is right. The I.T. authorities found that the assessee was carrying on the business of smuggling. They held that he was, therefore, liable to income-tax on the income from that business. On the basis that such income was taxable, the question is whether the confiscation of the currency notes entitles the assessee to the deduction claimed. The currency notes carried by the assessee across the border constituted

the means for acquiring gold in Pakistan, which gold he subsequently sold in India at a profit. The currency notes were necessary for acquiring the gold. The carriage of currency notes across the border was an essential part of the smuggling operation. If the activity of smuggling can be regarded as a business, those who are carrying on that business must be deemed to be aware that a necessary incident involved in the business is detection by the customs authorises and the consequent confiscation of the currency notes. It is an incident as predictable in the course of carrying on the activity as any other feature of it. Having regard to the nature of the activity possible detection by the customs authorities constitutes a normal feature integrated into all that is implied and involved in it. The confiscation of the currency notes is a loss occasioned in pursuing the business: it is a loss in much the same way as if the currency notes had been stolen or dropped on the way while carrying on

> the business. It is a loss which springs directly from the carrying on of the business and is incidental to it. Applying the principle laid down by this Court in **Badridas Daga v. CIT (1958) 34 ITR 10**, the deduction must be allowed."

11. The Apex Court further noted that in **CIT v. S.C. Kothari (1971) 82 ITR 794**, it had held that for the purpose of section 10(1) of the Indian I.T. Act, 1922, a loss incurred in carrying on an illegal business must be deducted before the true figure of profits brought to tax can be computed. **Grover J.**, speaking for the court, observed (p.802);

> "If the business is illegal, neither the profits earned nor the losses incurred would be enforceable in law. But, that does not take the profits out of the taxing statue. Similarly, the taint of illegality of the business cannot detract from the losses being taken into account for computation of the amount which can be

> subjected to tax as 'profits' under section 10(1) of the Act of 1922. The tax collector cannot be heard to say that he will bring the gross receipts to tax. He can only tax profits of a trade or business. That cannot be done without deducting the losses and the legitimate expenses of the business.

12. The Apex Court also noted in **Piara Singh**'s case that the Revenue had placed reliance on its judgment in the case of **Haji Aziz and Abdul Shakoor Bros. v. CIT (1961) 41 ITR 350 (SC)**. The Supreme Court pointed out that in that case, the assessee carried on the lawful business of importing dates from abroad and selling them in India. The import of dates by steamer was prohibited. Nonetheless he imported dates from Iraq by steamer, and the consignments were confiscated by the customs authorities. But the dates were released subsequently on payment of fine. The assessee's claim to deduction under s.10(2)(xv) of the Indian I.T.Act, 1922, was rejected on the ground that the amount was paid by way of penalty for a breach of the law. The

Apex court explained that "an infraction of the law was not a normal incident of business carried on by the assessee, and the penalty was rightly held to fall on the assessee in some character other than that of a trader."

13. Dealing with the reliance placed by the revenue on the case **Soni Hinduji Kushalji & Co. v. CIT (1973) 89 ITR 112 (AP)** in which case the assessee's claim to the deduction of the value of gold confiscated by the customs authorities was found unsustainable by the Court, the Supreme Court noted that "the decision in that case can be explained on the ground that the assessee was carrying on a lawful business in gold, silver and jewellery and committed an infraction of the law in smuggling gold into the country."

14. Referring to the reliance placed by the Revenue on the case of **J.S. Parkar v. V.B. Palekar (1974) 94 ITR 616 (Bom.)**, the Apex Court noted that in that case there was a difference of opinion between two learned judges of the Bombay High Court. A third learned Judge

agreed with the view that the value of gold confiscated by the customs authorities in smuggling operations was not entitled to deduction against the estimated and assessed income from an undisclosed source. The Apex Court further noted that in that case, the Bombay High Court had "observed that the loss arose by reason of an infraction of the law and as it had not fallen on the assessee as a trader or business man a deduction could not be allowed." The Apex Court finally noted that "the true significance of the distinction between an infraction of the law committed in the carrying on a lawful business and an infraction of the law committed in a business inherently unlawful and constituting a normal incident of it was not pointedly placed before the High Court in that case."

15. After explaining and distinguishing the various cases referred to and relied upon by the Revenue in **Piara Singh**'s case, the Apex Court negatived the contention of the Revenue and affirmed the view taken by the Punjab and Haryana High Court and allowed the deduction of Rs.65,500/- which was confiscated from

Piara Singh while smuggling the same across the border, as a business loss.

16. In the case on hand it is the contention of the Revenue that since that the assessee was admittedly not a smuggler and not carrying any illegal business of smuggling, that smuggling was not the business of assessee and therefore, he was not entitled to deduction of Rs.4,56,980/- being equivalent of foreign currency seized from him. However, learned Counsel for the Revenue has pointed out that although the Assessee had denied before the customs authorities that he was smuggler and was carrying the foreign currency as a part of his smuggling activities, the fact remained that customs authorities confiscated the same as currency being smuggled and also levied penalty of Rs.1,50,000/- thereby treating him as smuggler. Further, it is pointed out that this High Court in the Criminal Writ Petition/Application No.33/82 filed by the assessee challenging his detention under Cafeposa, has confirmed that the detenue/the petitioner i.e. the assessee herein was a member of a gang involved in smuggling.

The Assessee has produced a copy of the Oral Judgment dated 18th March, 1982 passed by this Court in the said petition. Para 5 of the said order of this Court reads as follows :-

> "This is a case of conspiracy wherein more than one person was involved in smuggling. The detenu is a member of group of conspirators, but the detention order is solely based on a finding that the foreign currency found belonged to the detenu and not to Aboobakar. Though in the grounds of detention it is stated by the detaining authority that the detenu was smuggling the currency out with Aboobakar, who was a co-conspirator, his case was not considered for detention either because there was no proposal or for the reason best known to the detaining authority. Unless the whole material against aboobakar was considered, a conclusion could not have been reached as to whether it was the detenu alone who was responsible for smuggling and the foreign

> currency did not belong to Aboobakar and belonged only to the detenu. It is no doubt true that it is not necessary in a case of conspiracy that a finding should be recorded before the detention order could be issued because every member of conspiracy is equally responsible and liable for the act of co-conspirator. But in this case the detention order is not based on conspiracy or the part taken by the detenu in conspiracy. It is based on a finding that the foreign currency found belonged to the detenu and not to Aboobakar who was alone co-conspirator."

17. Thus, it is seen that although the assessee has before the customs authorities denied that he was carrying on the business of smuggling and that foreign currency seized from Aboobakar belonged to him, the fact remains that the assessee was treated as smuggler, his subsequent detention under Cafeposa confirmed that he was treated as smuggler and the business of the assessee was that of smuggling and therefore, the foreign

currency recovered from Aboobakar, a co-conspirator of the assessee was the amount involved in the smuggling activity and the confiscation of the said amount was, therefore, business loss suffered by the assessee in conducting his business of smuggling. It may be noted that it is not the case of the revenue that the assessee was carrying on any other business, lawful as otherwise, for which the foreign currency was being illegally transported out the country. The business of the Assessee was smuggling of foreign currency, the confiscation of foreign currency equivalent to Indian Rupees 4,56,000/- was, therefore, a loss of stock-in-trade of the assessee. The Revenue while bringing to tax the sum of Rs.4,56,980/- as income of the assessee under Section 69A, can not deprive the assessee the benefit of treating the said amount as a business loss.

18. Accordingly, we hold that the assessee shall be entitled to the benefit of treating the sum of Rs.4,56,980/- confiscated from him as of business loss and answer the question referred to us for opinion in

the affirmative in favour of assessee and against the revenue.

**(A.S. AGUIAR, J.)** **(V.C. DAGA, J.)**